

**MINUTES  
of the  
FIRST MEETING  
of the  
REVENUE STABILIZATION AND TAX POLICY COMMITTEE**

**May 14, 2013  
Room 307, State Capitol  
Santa Fe**

The first meeting in 2013 of the Revenue Stabilization and Tax Policy Committee (RSTP) was called to order by Senator Carlos R. Cisneros, chair, on Tuesday, May 14, 2013, at 10:06 a.m. in Room 307 of the State Capitol in Santa Fe.

**Present**

Sen. Carlos R. Cisneros, Chair  
Rep. Edward C. Sandoval, Vice Chair  
Sen. Sue Wilson Beffort  
Rep. Anna M. Crook  
Rep. Brian F. Egolf, Jr.  
Sen. Timothy M. Keller  
Rep. Rodolpho "Rudy" S. Martinez  
Sen. Mark Moores  
Sen. Clemente Sanchez  
Sen. William E. Sharer  
Sen. John Arthur Smith  
Rep. James R.J. Strickler  
Rep. Thomas C. Taylor  
Rep. Jim R. Trujillo

**Designees**

Rep. Ernest H. Chavez  
Rep. Dennis J. Roch  
Sen. Nancy Rodriguez  
Rep. Luciano "Lucky" Varela

**Absent**

Rep. Henry Kiki Saavedra  
Sen. Lisa A. Torracco  
Sen. Peter Wirth  
Rep. Bob Wooley

Rep. Donald E. Bratton  
Sen. William F. Burt  
Sen. Jacob R. Candelaria  
Rep. Miguel P. Garcia  
Sen. Phil A. Griego  
Rep. Jason C. Harper  
Rep. Sandra D. Jeff  
Sen. Gay G. Kernan  
Rep. Tim D. Lewis  
Rep. Bill McCamley  
Sen. George K. Munoz  
Rep. Paul A. Pacheco  
Rep. Debbie A. Rodella  
Sen. John M. Sapien

Rep. Carl Trujillo  
Sen. Pat Woods

**Staff**

Damian Lara, Staff Attorney, Legislative Council Service (LCS)  
Tessa Ryan, Staff Attorney, LCS  
Pam Stokes, Staff Attorney, LCS

**Guests**

The guest list is in the meeting file.

**Handouts**

Handouts and other written testimony are in the meeting file.

**Tuesday, May 14****Interim Committee Procedures**

Raúl E. Burciaga, director of the LCS, reviewed some protocols particular to the RSTP. Mr. Burciaga explained that a statutory blocking provision applies; that is, if a majority of the members from a chamber rejects a proposed action, then it fails. The RSTP is also distinct in that it does not have advisory members, but designees. A quorum of the RSTP, which is composed of 18 members, forms when at least 10 of its members or designees are present.

Mr. Burciaga highlighted protocols applicable to all interim committees. A quorum is presumed to exist unless the issue of its nonexistence is raised. If it is acknowledged that a committee lacks a quorum, it may operate as a special subcommittee and accept testimony, but not formally act. Other standard rules are: the committee may act by consensus and a formal action requires a motion and a voice, hand or objection vote; absent approval from the New Mexico Legislative Council, the committee must meet in Santa Fe after September 30; and a legislator may be compensated for attending a maximum of four meetings of committees of which the legislator is not a member.

Mr. Burciaga distributed a calendar of interim committee tentative meeting dates that was created with the goal of minimizing scheduling conflicts for committee members and staff. He encouraged members to express their communication preferences to committee staff so that staff can effectively plan meetings.

A member suggested that the staff consider ways in which the RSTP might collaborate with other committees that focus on topics that the RSTP addresses, such as the Transportation Infrastructure Revenue Work Group and the Jobs Council. Another member asked that members receive a list of interim committee names and abbreviations.

## **Post-Session Fiscal Report**

David Abbey, director, Legislative Finance Committee (LFC), summarized the state's fiscal status. He characterized the 2013 legislative session as, generally, a success. Lawmakers enacted a balanced budget for fiscal year 2014. Spending of \$5.88 billion from the general fund, which includes capital appropriations of about \$510 million, increased by 4.3% from fiscal year 2013. Projected reserves exceed 10%. A major tax reform package, also signed into law and that generally adheres to the principles of good tax policy, will phase in a corporate income tax cut and phase out certain corporate income tax loopholes. When implemented, the session's tax legislation should initially increase and then gradually reduce general fund revenue. Mr. Abbey indicated that the reduction is cause for concern.

Mr. Abbey summarized revenue trends and forecasts. In the past several fiscal years, there were dramatic swings in revenue and appropriation levels; potentially deeper declines were tempered by the injection of federal money and the capture of unused capital appropriations. Overall, fiscal year 2014 revenues and spending reflect a relative return to pre-recession impact levels. Oil and natural gas prices and production levels, which have a tendency to fluctuate rapidly, have closely matched forecasts and will continue to be monitored attentively.

Changing revenue forecasts and other developments posed challenges in budget formation during the periods leading up to and into the session. "New money" projections increased slightly from August to December and then dropped mid-session. Further complicating budget matters were: a \$70 million set-aside to account for possible discrepancies between cash account and bank balances; potential liability for not maintaining adequate special education spending; the state's commitment to expand Medicaid pursuant to the federal Patient Protection and Affordable Care Act; and concerns about federal sequestration.

Ultimately, the LFC's total for recommended appropriations differed by \$1 million from that of the Department of Finance and Administration (DFA). The LFC recommended concentrating spending in the areas of Medicaid, education, public safety and general fund liabilities.

Certain categories of spending received more general fund money from the General Appropriation Act of 2013 than in fiscal year 2013: public schools, higher education, Medicaid, public safety and other categories. Public schools will receive the greatest share of additional funding, a 4.6% increase from the fiscal year 2013 appropriation of \$112.1 million. The public school increase, in part, is for satisfying special education maintenance of effort requirements; meeting increased formula funding demands; and programs that target early childhood services, particularly those that bolster reading and math proficiency. Meanwhile, higher education institutions will receive an additional \$38.2 million, or 5% more than in fiscal year 2013. In this area, the General Appropriation Act of 2013 emphasizes outcomes in degree completion; science, technology, engineering and math (STEM) degree awards; and the participation of minorities in STEM programs. Increased Medicaid spending reflects Medicaid expansion, a development that, despite some associated uncertainty, is expected to attract enough federal

dollars to generate a net gain in revenue over time.

Mr. Abbey highlighted other pieces of legislation that will affect fiscal resources. New formulas for the unemployment compensation insurance program will generate more revenue and improve the solvency of the program's fund. Modifications to the educational retirement and the public employees retirement programs will improve those programs' funds' solvency. Meanwhile, having not been changed through legislation, the Retiree Health Care Fund's solvency remains a concern. The Lottery Tuition Fund and Judicial Retirement Fund solvency and federal transportation funding are other areas of concern that will need to be addressed in future legislative sessions.

Questions and comments from committee members included the following.

- The estimated range of liability for the issues with the Statewide Human Resource, Accounting and Management Reporting System (SHARE) and cash reconciliation is between \$70 million and \$400 million. The cost of conducting the reconciliation, a necessary step, will be between \$600,000 and \$1 million. Updating SHARE at a cost of about \$10 million will help to prevent similar problems.
- The Public Education Department has not received a decision on its appeal for a waiver by the federal government of the state's past underfunding of special education. It might take a long time for the state to know its precise liability.
- How much of the state's revenue derived from, and what is the primary source of, reversions? How does the amount compare with other years? In fiscal year 2012, there was about \$66 million in reversions. The primary sources of that revenue were employee vacancies, unneeded capital outlay funding and savings from efficiencies realized through programs such as SHARE. The reversion amount fluctuates from year to year, but it ordinarily ranges from about \$40 million to \$50 million.
- For a host of reasons, the lottery scholarship program is facing insolvency. The cost of tuition, which is rising, is linked to the cost of the program; meanwhile, the rate of lottery play is stagnant. What can the legislature do to intervene? Because the cost of tuition has a direct impact on the Lottery Tuition Fund, the legislature might consider taking a tuition credit against increases of tuition in order to persuade universities to keep tuition low or prevent tuition increases.
- What is the effect of the partial veto of the appropriation to the Department of Information Technology for an upgrade to SHARE? The governor's veto struck a contingency related to certification by the Information Technology Commission, but that certification is otherwise required by law. The partial veto, then, is probably without effect.
- The federal government's full payments for Medicaid expansion might not

materialize because of sequestration. It may be useful to consider the possibility of modifying gross receipts tax exemptions in order to make up for potential federal payment shortfalls.

### **Organizational Business — Work Plan and Meeting Schedule**

Mr. Lara presented the committee's proposed work plan and meeting schedule for the 2013 interim. Members recommended the addition of several items and then adopted the plan. In the 2013 interim, the committee will:

1. examine the tax code and all other taxes not compiled in the tax code and discuss each tax based on the contribution to state revenue made by each tax and the adherence of each tax to the sound tax policy principles of:
  - (a) adequacy;
  - (b) efficiency;
  - (c) equity;
  - (d) simplicity; and
  - (e) accountability;
2. review the revenue status of the state, examine current revenue sources and discuss changes to revenue sources to ensure adequacy of revenue, including tax preparation fraud and the effectiveness of Taxation and Revenue Department (TRD) oversight and enforcement of tax collection;
3. review the effectiveness and value to the state of tax incentives, suggest changes to achieve state goals, including the benefits of transferability of income tax credits, and observe progress on projects benefiting from tax incentives;
4. continue to examine exemptions, deductions and credits to determine the ability to report and track the effectiveness and value to the state of tax incentives;
5. review the capital outlay process, the balances remaining in outstanding projects and the estimates of funds previously appropriated and available for future projects and discuss proposed changes to improve the process;
6. review trends in state investment earnings, including trends in the balances of the Severance Tax Permanent Fund and the land grant permanent funds and review the revenue received by the state from gaming within the state and the progress of tribal-state gaming negotiations;
7. determine legislative actions necessary to implement changes identified by committee members that will improve the tax system in New Mexico, including consideration of:

- (a) increasing the working families tax credit;
- (b) achieving revenue adequacy for the State Road Fund;
- (c) addressing the limitation on property tax valuations and resulting property tax lightning;
- (d) responding to congressional action to allow state taxation of remote sellers and internet sales; and
- (e) formalizing procedures to provide more accurate and timely fiscal impact reports (FIRs) that might also provide dynamic scoring;

8. evaluate recent tax and revenue-related legislation introduced in an effort to reduce ambiguity, mitigate unintended consequences and ameliorate deficiencies;

9. review the revenue status of gaming within the state, including lottery gaming, Indian gaming and gaming conducted by racinos and fraternal and other organizations; and

10. coordinate, as needed, with other committees regarding presentation of subject matter of common concern, particularly regarding sources of revenue that can be used to support transportation needs in New Mexico. The committee will hear a final report from the Transportation Infrastructure Revenue Work Group regarding its recommendations and proposed action.

Questions and comments from committee members included the following.

- The revenue derived from the Indian gaming compacts and other gaming activities is significant to the state; therefore, the RSTP might collaborate with the Committee on Compacts, if the Committee on Compacts meets. In any case, the RSTP will review the revenue status of gaming within the state, including lottery gaming, Indian gaming and gaming conducted by racinos and fraternal and other organizations, during the 2013 interim.
- The RSTP needs accurate FIRs in order to assess proposed legislation and should work closely with the LFC and various departments to get all FIRs as soon as possible with the proposed legislation presented to the committee.

### **Taxation of Internet Sales/Remote Sellers**

Richard Anklaam of the New Mexico Tax Research Institute updated the committee on online sales taxation compliance and legislative changes that might become necessary, a topic that he presented to the RSTP in October 2012. He noted that changes to his original presentation are marked with striking and underscoring.

The key legal issues related to states' ability to tax internet sales by remote retailers to in-state buyers are whether a state has jurisdiction, or nexus, over the seller and whether tax compliance is unduly burdensome. Increasingly, businesses have nexus with states because of in-state physical presence. The Marketplace Fairness Act (MFA) being considered by Congress

would constitutionally grant states the option to tax even more online retailers, many of which lack in-state physical presence.

Mr. Anklaam addressed other features of the MFA and its status. It would exclude from its provisions businesses that have less than \$1 million in United States sales. It would require states to provide detailed rate and boundary information and hold harmless any taxpayer that relies on that information, if incorrect. A state would have the option to collect local, not just state, taxes. Nevertheless, there is a strong indication that the MFA in its current form will not progress through the House of Representatives; changes to the bill are expected.

Mr. Anklaam discussed legislative changes that might be required for the state to tax pursuant to the MFA. Since the state generally does not tax based on destination, it might need to adopt an origin-based sourcing system. Bifurcating the sourcing rules — that is, having a set of rules for remote sellers and another for in-state sellers — would probably be acceptable. Though much of what will be required is subject to change, it nonetheless seems clear that the state will have to provide information on taxes required to be paid and furnish software to facilitate those payments.

United States Senator Mike Enzi, sponsor of the MFA, provided additional clarification in a response to a letter. Mr. Anklaam noted that most significant for New Mexico is that the MFA contemplates the gross receipts tax and its collection if the state adheres to the simplifications and protections provided in the MFA.

Questions and comments from committee members included the following.

- How much is New Mexico losing from untaxed online sales? One study has estimated losses at around \$70 million, but the study did not consider the small business exception, which would reduce that amount.
- Who would enforce compliance with the tax? The state would ensure compliance by out-of-state retailers. Since many of these retailers are already obligated to pay taxes to the state, the state's current efforts would expand.

### **2013 Tax Legislation: New Mexico Jobs Package**

Secretary Tom Clifford of the DFA spoke about recently enacted laws with fiscal impact, revenue trends, revenue forecasts and fiscal challenges. Despite challenges faced leading up to and during the session, lawmakers were able to compromise and enact several important pieces of legislation. Revenue- and spending-related challenges — many of which persist — included cuts in federal laboratory, military and education spending; mandatory increases in pension contributions; threat of insolvency of the unemployment insurance and employee health programs; and the need for critical upgrades to information technology systems.

Secretary Clifford highlighted several legislative measures with fiscal impacts. The

unemployment insurance program and the public employee pension program were reformed so that, although the programs might warrant future changes, improvements are expected. The lottery scholarship program, which received stop-gap funding, will require future action to become solvent. Capital outlay appropriations, the result of a legislative/executive compromise, provided funding for statewide and local projects, including development of water supply and tribal infrastructure and voting system modernization.

A major session accomplishment was the tax reform package. It reduces the corporate income tax rate to align more closely with rates of — and make New Mexico more competitive with — other states. The package also features a narrowing of the gross receipts tax deduction for manufacturers; mandatory combined reporting for most "big box" retailers; tightening of the high-wage jobs tax credit; an expansion and streamlining of the process for receiving the film tax credit; and the phase-out of local government hold-harmless distributions coupled with a new local option tax. Twelve counties and 20 cities, because of their size, will be particularly affected by the hold-harmless provisions. Secretary Clifford indicated that he will provide to LCS staff tables that illustrate in detail the anticipated impacts of those provisions.

Secretary Clifford discussed the need for the tax package, the need for diversification of the state's economy and the sustainability of the tax reform. New Mexico's per capita income and manufacturing levels fall below national measures, and its recession has lasted longer than the nation's. Meanwhile, two of the state's prominent revenue sources, federal funding and oil and gas revenues, have become tenuous: competition for federal funding has stiffened and oil and gas prices fluctuate unpredictably. The tax package, aimed in part to address these issues, can be sustained with less than 10% revenue growth and, hence, is affordable.

The levels of forecasted general fund revenue growth for fiscal year 2013 have been modified to reflect observed developments. The anticipated growth in most categories of revenue, excluding income taxes, has decreased. These lower expectations result largely from cuts in federal oil and gas leasing payments, high refundable tax credit claim levels and weak inflation. Countering these trends, oil and gas revenues have been relatively strong, and the number of issued housing permits has risen. Forecasted growth in fiscal year 2014 is 3.9%.

Secretary Clifford identified some foreseeable budget issues. They include: federal sequestration; special education maintenance of effort liabilities; the potential for weak federal Medicaid funding; lottery program solvency; and the effect of the hold-harmless provisions on local governments. Secretary Clifford added that the governor's recent executive order conditioning receipt of fiscal year 2014 capital outlay appropriations on compliance with the Audit Act has prompted the DFA to assist those appropriations' recipients.

Some tax policy concerns are: implications that would arise from the MFA's passage; the need for independent tax hearing officers; the income tax exemption for military pensions; new jobs tax incentives and tax relief for the research and design and small business sectors; property tax lightning; and dynamic scoring to fully assess the impact of tax incentives and their



effectiveness.

Questions and comments from committee members included the following.

- A problem plaguing economic development — one that tax incentives cannot overcome — is the low quality of the state's work force. Funding for education is about average among the states, yet academic performance is below average. More and more, colleges are offering remedial courses in response to need. These facts foster a negative perception of the state among potential employers. Secretary Clifford responded that he has met with the secretary of higher education, who in turn is working with economic developers, to discuss some of these issues. They have considered implementing an outcome-based funding formula and increased funding for bridge schools.
- The tax reform package's hold-harmless distribution curtailment could be very harmful to affected local governments. On the other hand, adjusting related provisions at the next session carries risk.
- When the new, stricter Governmental Accounting Standards Board rules take effect in fiscal year 2015, will the unfunded liability percentage drop from its current level of 91%? Most likely, but the degree of change will depend on the Public Employees Retirement Fund's performance.
- Is there an executive plan to restore the lottery scholarship program to long-term solvency? Can the tuition rate be changed to immediately improve the program's solvency? Consensus around the issue needs to be built soon so that measures to improve the program's solvency can be taken next session. Secretary Clifford commented that the DFA is reviewing proposals made during the session and would like to build consensus on a chosen pursuit. The tuition rate cannot be adjusted in time for the fall because the rate must by law be published by June 1. Two options for dealing with the impending shortfall are to cut the rate of reimbursement or issue a supplemental appropriation.
- Does the DFA know the tax reform package's effect on long-term — approximately 15 to 20 years in the future — revenues? Secretary Clifford replied that that information is not immediately available, but he will try to relay it to the committee in the future. A member commented that forecasting the tax reform's effects on revenue generation is particularly difficult because baseline figures are not static.
- What are the circumstances around the recent letter from the federal Department of Housing and Urban Development to the state suggesting that the state has not properly overseen the Section 108 community development block grants loan guarantee program? Secretary Clifford said that he met with a regional representative who expressed concerns about procedural, but not substantive, issues. If found that the state has not exercised proper oversight, future funding would be withheld. The state is working on a response to the letter,

which Secretary Clifford will present to the committee.

- A member solicited a response from Secretary Clifford about information regarding the tax reform package communicated to the House of Representatives by Secretary Clifford. On the last day of session, Secretary Clifford represented that the package would have a positive revenue effect for each of its first five years in law; updated reports cite a negative downturn in that time. Secretary Clifford responded by stating that, regrettably, his initial calculation was erroneously based on a different variable — that the hold-harmless distributions would be phased out at a more rapid rate — that was in an earlier version of the bill, but did not make it into the final version enacted.
- How many — and which — local governments will be impacted by the governor's recent executive order? About 60 of the 670 local governments are at risk of not receiving capital outlay appropriations. Secretary Clifford indicated that he will prepare and provide to staff a list of affected recipients for distribution to members.

### **2013 Tax Legislation: Impacts and Implementation**

Demesia Padilla, secretary, TRD reported on recent bills signed into law and other developments affecting the department.

New laws include provisions that:

- allow for the transfer of gross receipts liability from a utility seller to a manufacturer buyer, which will improve the ease of implementation of an existing anti-pyramiding measure;
- phase out hold-harmless distributions and allow local governments to impose additional gross receipts tax, on which the TRD is educating local government representatives;
- limit the credit that a taxpayer can receive on taxes paid to another state;
- create an option for taxpayers to contribute to the Horse Shelter Rescue Fund;
- create a tax incentive for corporations to establish nonretail operations that employ at least 750 in-state workers;
- permit manufacturing companies to use a single sales factor apportionment method in calculating income tax liability;
- tighten the definition of "consumable" in relation to gross receipts tax deductions to exclude — and therefore require tax payment on — tangible personal property used in the generation of power, the processing of natural resources and the preparation of meals;
- with certain exceptions, require the Property Tax Division of the General Services

Department to conduct at least one sale in each county in which there are delinquent tax payment properties; and

- change the application deadline for a landowner who wishes to qualify for the agricultural tax valuation method from the last day of February of the tax year to 30 days after the date of mailing a notice of valuation.

Secretary Padilla also commented that the TRD has been meeting target time line and budget marks on its upgrade to the GenTax System, a computer application that performs many of the TRD's functions. Upon completion, the system will be more efficient and effective, particularly in the area of taxpayer compliance.

The TRD is also exploring the possibility of using independent tax hearing officers. Taxpayers have complained about conflict of interest and fairness issues in the hearing process.

Questions and comments from committee members included the following.

- What retailers will be exempt from the combined reporting requirement of the tax reform package? Will that requirement apply, as was intended, to wholesale clubs, which could be considered both distribution centers and sellers to the end user? Secretary Padilla responded that the requirement does not apply to a corporation that employs at least 750 people in the state in a nonretail capacity. As with all tax laws, reasonable minds can differ in interpretation; the TRD's audit and protest hearing systems can be used to provide clarification. A member commented that it would be helpful to know more in the fall about how this aspect of the package will be officially interpreted so that the legislature might modify it, if needed, next session. Another member suggested that the TRD consider clarifying the issue through rulemaking.
- A member requested that the TRD disclose to the committee both the number of corporations that changed their filing to the combined reporting method and the revenue impact of the shift when that information is available. Secretary Padilla indicated that she will provide the information to the extent that she can without revealing taxpayer identity.
- Prompted by an earlier discussion about the likely usefulness to the committee of pre-session access to FIRs on tax legislation, a member asked Secretary Padilla about the feasibility of producing analysis during the interim. Secretary Padilla responded that the division that handles FIRs is fully staffed and the TRD would welcome receiving requests for analysis ahead of session. She added that it would help the TRD to be able to anticipate the legislature's priorities and the level of complexity of requests for analysis so that TRD staff could effectively prepare for session requests.

There being no further business, the committee adjourned at 2:29 p.m.